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RESEARCH ARTICLE
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Article 2 of Double Taxation Agreements and the Fate of Digital Service Taxes

Mustafa Cemil Kara[*]

Abstract

Article 2 of double taxation agreements (DTAs) is intended to ensure covered taxes under a DTA. Article 2 is significant since the legal protection provided by DTAs is limited only to the scope of DTAs. However, the wording of Article 2 may lead to confusion and uncertainty for taxpayers in terms of taxes within the scope of DTAs. In recent years, there has been a widespread trend of excluding digital service taxes (DSTs) from DTAs due to the lack of a global consensus on a common solution. This has refocused attention on Article 2. The fact that there is a scarcity of research on Article 2 raises concerns about what will happen if different types of taxes emerge over time. In this article, some important points and Türkiye's approach related to Article 2 and Türkiye's DST law which sometimes causes ambiguities and uncertainties for taxpayers were highlighted. This article also aimed to enhance a common understanding of the logic of the term "taxes covered." The research employed the descriptive research method, primarily utilizing the OECD Model Tax Convention (MTC) and its commentary, as well as prominent academic studies in the field and the Turkish DST law.

Keywords: Double Taxation Agreement, Contracting State, Taxes Covered, Digital Service Taxes

JEL Codes: K34, H25, H26

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[*] Dr., Head of Group, Turkish Revenue Administration, Ankara, Türkiye.
Email: mckara61@gmail.com, ORCID: https://orcid.org/0000-0003-3756-8719

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1. Introduction

Determination of "covered taxes" in a DTA is crucial since it reveals a framework for the taxes that a DTA covers. One of the purposes of DTAs is to provide taxpayers with certainty regarding the tax liabilities they may face in foreign countries. For this purpose, taxation power is shared between the contracting states or can be given exclusively to one of them. To effectively prevent double taxation, it is important to clearly determine the scope of taxes to which DTAs will apply. DTAs have a dual feature because they are both within the scope of international treaties and a part of the domestic legislation of the contracting states. Since country tax systems and their understanding of the tax concepts may differ, hesitations or implementation difficulties may arise regarding the scope of the taxes to which a DTA applies. The issue of "covered taxes" in DTAs may be the subject of controversy from time to time. Moreover, certain taxes such as DSTs can be difficult to determine whether they fall within the scope of the OECD MTC. Therefore, an examination of Article 2 of the OECD MTC is important for understanding whether DSTs or their equivalents are covered by DTAs in force.

Since the international tax treaty network is largely based on the OECD MTC, the texts of the OECD MTC and its Commentary are considered in this study. Article 2 of DTAs, titled "taxes covered," regulates the taxes to which a DTA will apply. The text of Article 2, broadly including taxes on income and capital, has been accepted in DTAs worldwide. For this reason, the article is considered one of the most important DTA articles. The contracting states reveal that they will use and share their taxation powers on what kind of taxes they want to include within the scope of the DTA. Article 2 clarifies the terminology and classification and makes specifications for the taxes covered while also extending the scope of application of the DTA by including the taxes imposed by the political subdivisions or local authorities of the contracting states as far as possible and in accordance with the internal laws of the states (OECD MTC Commentary on Art. 2, 2017, para. 1).

In addition, one of the functions of Article 2 is to eliminate the need to conclude a new DTA whenever the domestic laws of the states change, and to enable the contracting states to inform each other in case of significant changes (OECD MTC Commentary on Art. 2, 2017, para. 1).

In this article, some specific issues and Turkish approach related to the subject are evaluated by emphasizing the function of Article 2 in the implementation of DTAs. Another aim of this article is to reveal that the provisions of the DTA reflect a common understanding of the contracting states, also often called the common "international tax language." Additionally, the article examines and addresses the criteria that determine whether DSTs are included in or excluded from the scope of Article 2 of DTAs.

The article is divided into three parts. Section 2 considers the content and peculiarities of DTAs, in particular, the substantive scope of Article 2 of the OECD MTC. This section intends to explore the boundaries of Article 2, including important aspects on the matter of ordinary and extraordinary taxes in a DTA and the country reservations and Türkiye's approach regarding Article 2. Finally, Section 3 discusses the rationale behind the implementation of DSTs, followed by their application in Türkiye and the place of DSTs in the context of DTAs.

2. The Content and Peculiarities of Article 2 of Double Taxation Agreements

Taxes generally change and develop over time. Corporate income tax is also included and is the most traditional method of taxing company profits. However, there is a trend towards an ever-expanding corporate income tax base. With the evolution of corporate income tax, new tax forms come to the fore. These new tax forms can be described as "alternative or non-traditional" taxes. Although corporate income tax is generally collected by the traditional method, it can sometimes be collected on gross income, and sometimes it can display a hybrid appearance, intertwined with traditional corporate income tax and gross-based tax. Such taxes can be assessed either as an alternative to corporate income tax or in addition to corporate income tax. For example, revenue-based taxes, where the tax base is quite different from the calculated net profits, are on the agenda and may be subject to debate in terms of the implementation of DTAs (Grapperhaus, 2009, pp. 35−40; Tenore, 2012, p. 1).

Article 2(1)[1] of DTAs defines the subject of the DTA by providing that the DTA shall apply to "taxes on income and capital" respectively. Article 2(2)[2] sets out what taxes on income and capital include. The first and second paragraphs of Article 2 broaden the scope of DTAs by determining the taxes on income and capital. In these paragraphs, it is pointed out that all taxes collected on income or capital elements may be included, although these are not counted one by one (General Communiqué No 1 on Double Taxation Agreements, 1996). Since these paragraphs do not refer to domestic law, they must be interpreted without taking into account the domestic laws of the contracting states (Lang, 2005, p. 216). In Türkiye, income tax and corporation tax fall into the scope of DTAs. Indeed, it is possible to see two types of taxes mentioned by name in the DTAs signed by Türkiye (General Communiqué No 1 on Double Taxation Agreements, 1996). Besides income tax and corporation tax, it seems that the funds received due to these taxes have been included in Türkiye's old agreements (General Communiqué No 1 on Double Taxation Agreements, 1996). It needs to be noted that in Türkiye the fund share is no longer collected from the income and corporation tax amounts calculated on annual income and corporation tax returns since 2004. In general taxes on income are included in the scope of the DTAs to which Türkiye is a party.

In the first paragraph of Article 2, it is underlined that a DTA will apply to taxes on income or capital on behalf of a contracting state or its political subdivisions or local authorities, regardless of how the taxes are levied. It is emphasized that the taxes levied by the specified administrative structures will be included indiscriminately; in other words, the organizational structures of the administrations or the taxes for which authorities are levied do not matter (OECD MTC Commentary on Art. 2, 2017, para. 2). Thus, it is clarified that not only federal taxes but also taxes levied by federated states and municipalities are within the scope of a DTA (Lang, 2005, p. 217). However, there may be different practices regarding whether or not the local specific taxes applied by the federated states are included in a DTA (Pires, 1989, p. 227; Yaltı

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[1] "This Convention shall apply to taxes on income and on capital imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied."

[2] "This Convention shall apply to taxes on income and on capital imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied."

Soydan, 1995, pp. 114–115). As there is no political subdivision in Türkiye, such an administrative authority receiving tax on income and capital is not in question in terms of Türkiye. In addition, due to the lack of local governments' taxation power in Türkiye a tax levied in this way is not available (General Communiqué No 1 on Double Taxation Agreements, 1996). It is understood from the statement in the paragraph that the method of levying taxes is not important. In other words, the collection of taxes in the form of additional taxes or surcharges by direct accrual or witholding at source will not make any difference in terms of the scope of the tax.

In the second paragraph of Article 2,[3] all taxes imposed on total income, total capital or on items of income or capital, including taxes on profits arising from the disposal of movable or immovable assets, taxes on the total amount of wages or salaries paid by enterprises and taxes on capital appreciation are deemed to be taxes on income and capital. In the paragraph, it is seen that the definition of taxes on income and capital is made and it is understood that taxes will include the total income and income elements and those collected on the total capital and capital elements (OECD MTC Commentary on Art. 2, 2017, para. 3). Components of taxes on earnings are also covered by DTAs, such as taxes on gains from the alienation of movable or immovable property, taxes on the wages or salaries paid by enterprises, as well as taxes on capital appreciation (Ismer & Jescheck, 2017, p. 386). Those who have drafted this paragraph have discussed the subject in the broadest way and perspective possible (Jiménez, 2018, p. 167). On the other hand, social security premiums and any similar premiums directly linked to social assistance will not be considered as taxes on the total amount of wages and will therefore be excluded from the list of taxes (OECD MTC Commentary on Art. 2, 2017, para. 3). In the paragraph, only some income items are mentioned as it is seen unnecessary to count all income items one by one. It is also stated that all taxes collected on total income or income items are taxes on income. The reason for this can be stated as the fact that detailed regulations regarding the taxation of each income item have been made in the other articles of the DTA. As a matter of fact, it can be seen that some income items are arranged in different articles depending on the type of activity or who obtained them.

Besides, in the comment note of the second paragraph, it is emphasized that most states think that the interest and penalties concerning the related taxes are not covered by the article. However, if the taxation is cancelled or the amount of the tax payable is reduced in accordance with the mutual agreement procedure under Article 25 of DTAs, the same treatment should be applied to the interest and administrative penalties related to this taxation (OECD MTC Commentary on Art. 2, 2017, paras. 3-4).

By the way, it should be noted that contracting states frequently remove the reference to "*taxes on capital*" in the first and second paragraphs, limiting the scope of application to "*taxes on income*" only. To avoid the broad scope provided in the first and second paragraphs, the contracting states may narrow the scope of the DTA by waiving certain elements or by limiting the scope to certain taxes that are specifically enumerated.

[3] "There shall be regarded as taxes on income and on capital all taxes imposed on total income, on total capital, or on elements of income or of capital, including taxes on gains from the alienation of movable or immovable property, taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation."

In the third paragraph of Article 2,[4] it is ensured that the tax types to be applied by the DTA are listed by both contracting states. Contracting states list the taxes existing at the time of signature of the agreement. The term "*in particular*" makes it clear that the list is not open-ended (Ault, 1997, p. 386). In other words, the list is not exhaustive as it serves to illustrate the previous paragraphs of the article through examples (OECD MTC Commentary on Art. 2, 2017, para. 6). For this reason, it would be appropriate for the treaty negotiators to provide sufficient information to the other state about the current taxes applied in their own countries (Lang, 2005, p. 220). It is noteworthy that the third paragraph uses the phrase "*in particular*" and can be considered as a sign that the list may expand towards the relevant taxes (Lang, 2005, p. 220). The list in the third paragraph ensures that states and taxpayers have a correct idea about the scope of application of the DTA. Certain agreements do not include the phrase "*in particular*" in paragraph 3. In this case, the list can be interpreted more broadly. It is important what constitutes the tax base and how the tax base is calculated (Brandstetter, 2010, p. 122). In principle, this paragraph sets out a complete list of taxes applied in both states at the time of signing the DTA. Michael Lang thinks that this is a contradiction; in other words, the fact that on one hand there is no complete list and on the other hand this list should in principle be exhaustive may cause interpretation problems (Lang, 2005, p. 220). It is essential that the taxes included in this list are interpreted with their meanings when the DTA was signed (Lang, 2005, p. 216).

In the fourth and last paragraph of Article 2,[5] referring to the domestic legislation, it is foreseen that the DTA will be applied to the taxes of the identical or substantially similar scope in addition to or instead of the existing taxes in the contracting states after the signature date of the DTA. It can be said that the term "*substantially similar*" is based on the essence of the tax. In order to claim that any future tax meets the characteristics the taxes listed in the third paragraph, not a single feature of this tax, but its several important features will need to be evaluated together. If a contracting state changes an existing tax after signing the treaty, this new tax will also be within the scope of the treaty as long as it is substantially similar (Helminen, 2016, s. 2.2.2.2). With this provision of the article, in case of new tax incurrence in domestic law after the signing of the DTA, becoming inapplicable of the DTA and the trouble of changing it are avoided (Işık, 2014, p. 91). In other words, paragraph 4 aims to prevent the DTA from becoming unenforceable in case of changes in domestic legislations.

While the third paragraph only lists the relevant taxes, the fourth paragraph stipulates that all identical or substantially similar taxes that come into force in domestic legislation after the date of signature of the DTA are automatically within the scope of the DTA. Each state undertakes to notify the other of significant changes in tax laws if new taxes are introduced or if there are taxes replaced by new ones. However, it should be said that the DTA does not envisage a mechanism that will force the states to fulfill the conditions of the notification. The requirement of the state to notify the other state of changes in its domestic legislation can be derived from the application of the principle "*pacta sunt servanda*" that international treaties are binding and should be executed in good faith (Brandstetter, 2010, p. 44).

[4] "The existing taxes to which the Convention shall apply are in particular: a) (in State A): .... b) (in State B): ...."

[5] "The Convention shall apply also to any identical or substantially similar taxes that are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of any significant changes that have been made in their taxation laws."

2.1 The Matter of Ordinary and Extraordinary Taxes In A Double Taxation Agreement

The OECD MTC does not distinguish between ordinary and extraordinary taxes. That is to say, the article does not mention about ordinary and extraordinary taxes. Normally, the inclusion of extraordinary taxes in a model treaty may be justified, but experiences have shown that such taxes are often applied in very specific circumstances. They are also difficult to describe. These taxes can be extraordinary for various reasons such as their application, the way that they are charged to the taxpayer, their rates, and their purposes. In this case, it seems more appropriate not to include extraordinary taxes in the DTA. However, since extraordinary taxes are not intended to be excluded from all DTAs, ordinary taxes are not mentioned, either. Contracting states are thus free to limit the scope of application of the DTA to ordinary taxes or to extend it to extraordinary taxes, or even to impose special provisions (OECD MTC Commentary on Art. 2, 2017, p. 5).

It can be understood from the interpretation of the second paragraph of Article 2 that extraordinary taxes are covered by the DTA, unless the contracting states make a clear exclusion. On the other hand, a contracting state may also claim that extraordinary taxes will not be covered by the DTA in the absence of a special provision. Therefore, the focus should be rather on the writing of Article 2. From the current writing, it is not possible to make an impression that a tax is applied regularly or only in certain cases. There is no differentiation in ordinary and extraordinary taxes, and all tax types collected on income and capital can be covered by the DTA (Lang, 2005, p. 217).

2.2 The Country Reservations and Türkiye's Approach Regarding Article 2

Canada, Chile and the United States reserve their approach to paragraph 1 of Article 2, which states that the DTA should apply to the taxes of political subdivisions or local authorities. Besides, Australia, Japan and Korea reserve their approach to paragraph one, which states that the DTA should apply to taxes on capital. Greece and Latvia are of the opinion that taxes levied on the total amount of wages or salaries paid by enterprises should not be considered as taxes on income, and therefore should not be covered by the DTA (OECD MTC Commentary on Art. 2, 2017, paras. 10, 11, 12).

In addition, in the observation note put by only Portugal who does not agree with the last three sentences of the comment note (OECD MTC Commentary on Art. 2, 2017, para. 4) of the second paragraph of the article, Portugal recorded the view that interests and penalties are not included in the DTA and therefore cannot be handled within the scope of the mutual agreement procedure (OECD MTC Commentary on Art. 2, 2017, para. 9). Some countries, like Portugal, do not consider items such as interest and fines as taxes under Article 2. For this reason, it is important for countries to clarify this issue in negotiations (OECD MTC Commentary on Art. 2, 2014, para. 4).

The first paragraph of Article 2 of the DTAs states that it does not matter whether the taxes are taken on behalf of the state itself or, if any, its political subdivisions and local authorities. In Türkiye as there is no political subdivision, taxes on income on behalf of such a subdivision

is not applicable. Since local governments do not have a power to tax in Türkiye, the phrase "receiving taxes on behalf of local governments" does not make any sense.

Although it is stated in the first paragraph of Article 2 that the taxes collected on income are generally within the scope of the DTA and the taxes collected on income are defined in the second paragraph, the taxes that are applicable as of the signature date of the DTA and to which the DTA will be applied are listed by name in the third paragraph.

In accordance with the provisions of the third paragraph, the contracting states can include in the DTA the tax types that will be applicable among them. For example;

> The existing taxes to which the Convention shall apply are in particular:
> a) in State A:
> (i) Income Tax;
> (ii) Corporation Tax;
> (hereinafter referred to as "State A tax")
> b) in State B:
> (i) Income Tax;
> (ii) Corporation Tax;
> (iii) Capital Tax;
> (iv) Business Tax;
> (v) The Levy Imposed on Income and Corporation Tax
> (hereinafter referred to as "State B tax").

In addition, contracting states may agree to include special types of income taxes during DTA negotiations and include specific provisions regarding them in their DTAs. The provisions of the agreement are applied not only to the taxes specified in the paragraph above, but also to similar taxes created after the date of the agreement.

In Türkiye it is necessary to collect the earnings and revenues obtained by real persons from various income elements within a calendar year and to submit the calculated income to the tax office with a declaration.

In the first article of the Income Tax Law No. 193, income is defined as "The income of real persons are subject to Income Tax. Income is the total net earnings and profits of the real persons gained within a calendar year." In the second article of the same law, the income elements are counted as follows:

(1) Commercial earnings
(2) Agricultural earnings
(3) Remunerations
(4) Earnings from self-employment
(5) Immovable capital revenues
(6) Movable capital revenues
(7) Other earnings and revenues

In Article 1 of Corporate Income Tax Law No. 5520, it is stated that the earnings of the corporations listed below are subject to corporation tax:

(a) Incorporated companies
(b) Cooperatives
(c) Public economic enterprises
(d) Economic enterprises of associations and foundations
(e) Business joint-ventures

In the same article of the same law, it is stipulated that the corporation's income consists of the income elements that are the subject of income tax. In other words, corporation's earnings consist of components that fall within the scope of income tax.

Considering that the elements of income and capital covered in model tax agreements are generally listed as "income from immovable property," "business profits," "income from international shipping and air transport," "dividends," "interest," "royalties," "capital gains," "income from independent personal services," "income from employment," "directors' fees," "income of entertainers and sportspersons," "pensions," "income from government service," "students' income" and "other income"; it is seen that these are income items that fall within the scope of Turkish income tax and corporation tax.

On the other hand, even if taxes on income and capital fall into the scope of DTAs, there is no tax on capital in real sense in Türkiye. It should be noted that Türkiye does not have wealth taxes that fall within the scope of DTAs. In some of Türkiye's DTAs wealth taxes have been also included in the scope in case of wealth taxes applied in other contracting states (Öz & Çavdar, 2012, p. 60). In other words, if other countries with which Türkiye has the DTAs apply wealth taxes within the scope of the DTA, wealth taxes are also included in the scope of DTAs. However, DTAs essentially apply only to taxes on income in terms of Türkiye.

Last but not least, it is worth mentioning that if a capital tax or a wealth tax is introduced in the future in Türkiye, inheritance and transfer taxes are not among taxes on capital or a wealth in terms of implementation of DTAs (Turkish Revenue Administration's tax ruling, 2014).

In the next section of the article, the current status and fate of DSTs are examined. There are many who argue that DSTs are designed to circumvent DTAs. In the literature, it is debated whether DSTs are taken based on income or expenditures. The importance of interpreting and implementing DTAs in good faith paves the way for DSTs, which have the same effect as taxes on income, to be included within the scope of DTAs. However, it is clear that if states tax the cross-border commercial profits of businesses that do not have any permanent establishment in market countries under the name of DSTs, they will naturally violate DTAs. This argument actually has merit if DSTs are taxes on income on hidden business profits. As digital services have become an important part of the global economy, concerns are increasing about how country tax legislations and DTAs will adapt to this change.

3. The Emergence of Digital Service Taxes

The digital economic activities continue to develop in line with the globalization process, while leading to international cooperation and collaboration in the fields of economy, tax and law (Sağır, 2022, p. 53). The exponential rise of digital economic activities in the last 20 years in particular, has led to the problem of how such activities should be taxed. As digital services become increasingly widespread activities of the global economy, concerns have arisen about how tax systems will adapt to this change (Karnosh, 2021, p. 513). This is because new business models have emerged in the world with the development of the digital economy, and the legal rules associated with a period based on physical presence in economic relations have been insufficient in the face of such developments (Çelener, 2019a, p. 2228). The definition specified for the type of activity or transaction may be either extensive or limited; for instance, a

definition that includes different layers of economic activity such as architecture, engineering, trade, transportation, marketing, advertisement, information services, government services, health, education, etc. would be deemed extensive, whereas a definition that includes only electronic delivery would be qualified as limited (Yaltı, 2003, p. 3).

With digital technologies enabling more transactions than ever before, it is now evident that the digital economy is increasingly playing an integral part in the functioning of the economy as a whole (UNCTAD, 2019, p. 4). In particular, the widespread use of mobile devices and the internet has expedited this process (Ferhatoğlu, 2018, p. 212). This profound breakthrough in information technologies and digitalization poses a grave threat to the taxation authority exercised by countries (Ekmekçi et al., 2020, p. 109).

The digital economy operates almost entirely in a virtual environment, whereas existing international tax law rules focus on the physical place of business. As a matter of fact, there is a huge income in this environment and it is necessary to tax this income to ensure tax justice and protect countries' tax revenues (Demirhan, 2020, p. 85). Unfortunately the traditional rules of the international tax system have failed to address the digital economy.

It has been frequently stated that while multinational corporations (MNCs) generate income in the countries where they operate, they are not taxed in the same manner as companies established in said countries since they do not own any physical assets, leading to tax injustice and tax losses for the countries of origin. Given that the inadequacy of existing international tax rules has led to major base erosion and profit shifting (BEPS) opportunities in the digital economy, the necessity of taxing profits where economic activities are engaged and value is generated has been a key subject of the international tax agenda in recent years (Kara, 2022, p. 291). In response to the BEPS efforts of multinational companies, states are increasingly trying to supplement their corporate income taxes with new type of taxes (Ismer & Jescheck, 2018, p. 573). Put differently, there is a general international acknowledgement that digital services should be taxed in the countries where they are generated, since their costs are low while their profits are very high (Karabulut, 2020, p. 270).

The OECD has been working on BEPS since 2013 and has developed a project called the BEPS Project. The action step on taxation of the digital economy, the first of the actions in the BEPS Project, for which a final report was published in 2015, has not yet been finalized. The countries adopted their own unilateral measures as the search for a common solution within the OECD dragged on. The DST has already been implemented by several OECD countries after it was first recommended in March 2018. For instance, the United Kingdom (UK) introduced a 2% DST to take effect in April 2020. As per the regulation, companies with worldwide revenues exceeding £500 million and UK revenues exceeding £25 million shall be subject to this tax. Italy, on the other hand, introduced a DST of 3%, which would enter into force at the beginning of 2020. France introduced the DST retroactively, to take effect from the beginning of 2019 (Durdu, 2020, p. 1969). The countries that have implemented the DST within their sovereign jurisdiction are not limited to OECD countries, as a number of countries around the world have either started to adopt it or are planning to do so in case a global solution cannot be achieved. Thus, revenues from digital services provided by MNCs are taxed by several countries within the scope of digital tax policies, and this situation has evolved into a significant source of

international double taxation. It is indeed apparent that such unilateral tax measures also result in compliance costs and uncertainties for multinational corporations (MNCs) (Postler, 2020, p. 77). To summarize, the DST practices have initiated as of 2019 and 2020, and are still being implemented as a very new type of taxation (Kılıçer & Peker, 2021, p. 73).

It is also clear that the inability of countries to develop a common approach on how to tax revenues from digital economy activities has left countries to their own devices, resulting in varying tax rates (Erdem, 2016, p. 116; Kara & Öz, 2016, p. 32.). Moreover, unilateral measures contradict the principles of international taxation, such as neutrality, certainty, fairness, and efficiency, while additional and heterogeneous taxes on the same transactions raise the risk of double taxation (Petruzzi & Buriak, 2018, sec. 2.4.7).

The fact that countries have escalated their pursuit of tax revenues from digital activities through unilateral measures has raised concerns among the global public opinion (Kara, 2022, p. 293). Moreover, the fact that the share sought by countries is higher than it should be has brought the need for a global consensus-based sharing in this area into the spotlight (van den Hurk, 2020, p. 133). The unilateral measures taken by one country after another, leading to a complex tax system and posing a risk to the global economy, compelled the OECD BEPS Inclusive Framework (IF) to take the initiative and intensify its efforts for a global consensus-based solution (Postler, 2020, p. 76). Preventing unilateral measures is also acknowledged as a step in the right direction in ensuring tax certainty and eliminating international trade wars (Oguttu, 2020, p. 810).

Whether the DST is characterized as a direct tax or an indirect tax levied on services, the rightful demand of developing countries, as the source countries, that multinational companies generating profits from such services should pay taxes in the country in which those profits are generated will likely to endure (Sağır, 2022, p. 69). In this context; even though the DSTs unilaterally imposed by countries on digital service activities are intended to circumvent DTAs, the fact that such taxes have begun to be levied by several jurisdictions has forced countries to work and cooperate under the OECD/G20 leadership with regard to the payment of taxes by multinational corporations in the source country.

Likewise, the fact that the first action of the BEPS Project is devoted to solving tax problems arising from the digital economy indicates the significance attributed to the matter (Kara, 2022, p. 292). Furthermore, at the IF meeting held on October 8, 2021, 136 member countries of the IF, including Türkiye, agreed on the taxation of the digital economy based on the two main pillars, and a declaration concerning this subject was published on the same date (OECD/G20 BEPS Project-Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 2021, October 08). At the current stage, the search for a solution for the taxation of digital economy activities is projected as the removal of the DST and similar taxes imposed unilaterally by the countries with the signing of the aforementioned Multilateral Convention (MLC) in the second half of 2024 and its entry into force in the near future.

3.1 Application of the Digital Service Tax in Türkiye

The DST has been regulated under Law No. 7194 (2019) and entered into force as of 2020, March 01. As per Article 1 of the Law on Digital Service Tax and on Amending Certain Laws and Decree Law No. 375, titled "subject of tax," the subject of DST is the revenue obtained from all kinds of advertising services rendered in the digital environment; services rendered in the digital environment for the sale, listening, watching, playing or recording on electronic devices and use of any audio, visual or digital content in the digital environment; services rendered in the digital environment for the provision and operation of digital environments where users can interact with each other. In addition, the revenue obtained from the intermediary services rendered by digital service providers in the digital environment for the specified services shall also be subject to DST.

The taxpayer of the DST is the digital service providers. Whether or not they are full taxpayers in terms of Income Tax Law No. 193 dated 1960, December 31 and Corporate Tax Law No. 5520 dated 2006, June 13 and whether or not they conduct the activities in question within the scope of limited liability to tax through their workplace or permanent representatives in Türkiye does not affect their liability to the DST.

Taxpayers whose revenue obtained in Türkiye is less than 20 million Turkish liras or whose worldwide revenue is less than 750 million euros or the equivalent foreign currency equivalent of Turkish liras are exempt from the tax. The DST rate is set at 7.5%. While the DST poses as a direct tax given that it is intended to capture the earnings of the businesses within the scope of the tax, it is levied on the revenues obtained by multinational companies in return for the services rendered and is undoubtedly reflected to the beneficiaries of these services (Saraçoğlu & Kahraman, 2020, p. 13). The DST in Türkiye is a tax practice based on the approach of adopting unilateral measures for the taxation of digital services, with examples available around the world. It can be argued that the DST in force in Türkiye bears significant resemblance to other global examples and the practices in the EU countries.

With respect to the regulation in the Turkish legal system, it can be argued that the DST is levied on revenue, and thus it is a direct tax on income (Karabulut, 2020, p. 277). In line with this, subjecting limited taxpayers who do not maintain a permanent establishment in Türkiye to the DST shall contradict the DTAs. On the other hand, it can also be argued that the DST is, in fact, an indirect tax, as it is levied on the provision of a digital service (Mutlu Kaya, 2020, p. 460). However, it is evident that the categorization of the DST as an indirect tax is likely to render the prevention of double taxation exceedingly difficult (Çelener, 2019b, p. 50). Although the DST is calculated and paid on the taxpayer's revenue, it will likely be reflected on the consumer and the actual taxpayer will be the consumer, as in expenditure taxes (Mutlu Kaya, 2020, p. 460). In conclusion, it should be stated that the DST does not fit into the classical tax categorization with respect to its legal nature (Mutlu Kaya, 2020, p. 461).

The U.S. Trump Administration launching trade investigations against countries that levy DSTs on the grounds of discrimination against their own companies was the beginning of the end for DSTs. Following these investigations, the U.S. decided to impose additional customs duties on certain products in Türkiye, India, the UK, Italy, Spain, France and Austria. In this regard, a total of 32 products in the sectors of carpets, glass, ceramics and jewelry exported to

the US would be subject to an additional 25% tariff. As evidenced by the trade investigations launched, the US is committed to the elimination of unilateral measures such as DSTs and similar unilateral measures and to preventing the introduction of new ones. The Biden administration, on the other hand, suspended the planned tariffs in support of the OECD/G20 resolution process on international taxation of digital economy activities.

On October 21, 2021, the U.S. Department of Treasury announced that an agreement to eliminate digital service tariffs had been reached with Austria, France, Italy, Spain, and the UK, which currently impose such tariffs. On November 22, 2021, a joint statement announcing Türkiye's participation in this agreement was published on the website of the U.S. Department of Treasury. In summary, Türkiye would be entitled to maintain imposing the DST until the MLC entered into force. A portion of the DST accrued between January 01, 2022 and the date of entry into force of the MLC would be deducted from the corporate tax payable pursuant to the MLC. In other words, the transitional DST amount in excess of the first year's corporate tax amount calculated as per the new rule would be deducted from the corporate tax payable by the covered companies as per the new rule.

The MLC, which is expected to be available for signature in the second half of 2024, establishes a new taxation right to tax the profits of the largest and most profitable companies. In addition, the entry of the MLC into force marks the end of imposing the DST and similar unilateral measures. Türkiye is among the countries that have pledged their commitment to this effort, which was pioneered by the G20 and the OECD. Besides, it seems essential for Türkiye to accede to the MLC and adopt the required arrangements within the scope of the MLC with the aim of protecting Turkish export companies against the possibility of sanctions arising from the US trade investigation. Put differently, Türkiye is highly likely to face sanctions such as trade investigations and, ultimately, customs duty sanctions from the US should Türkiye refrain from acceding to the MLC and maintain the DST.

3.2 The Relevance of Digital Service Taxes in the Presence of International Tax Treaties

It is argued that a revenue-based tax may be subject to DTAs due to its substantial similarities to, if not the same characteristics as, income or corporate taxes. It is controversial whether a DST is a tax levied on income or on expenditure. The view advocating that a DST is a tax levied on income claims that a DST is a tax levied on income, similar to all other taxes levied on revenue. Since DTAs encompass all taxes levied on income, it can be argued that a DST is also covered within this scope. On the other hand, the view that a DST is a tax on expenditure argues that a DST is calculated by applying a proportional rate on revenue without any deduction from the tax base. Thus, this tax can also be referred to as a turnover tax. This approach essentially recognizes that a DST is not a tax on income, but rather an indirect tax (Oktay, 2020, p. 99; Sağır, 2022, p. 67). Taxes on expenditure are also not covered by DTAs.

In the categorization on the basis of the source or subject of the tax, a tax is characterized as an income tax when levied on a person's income, and as an expenditure/consumption tax when levied on goods or services subject to consumption (Şen & Sağbaş, 2016, p. 58). In the categorization with respect to the relationship between the tax and economic activity, taxes whose subject is continuous, whose taxpayer is predetermined, and whose tax base is

continuous are characterized as direct tax, while taxes whose subject and tax base are not continuous and whose taxpayer is not predetermined are characterized as indirect tax (Nadaroğlu, 1998, pp. 328−329). Accordingly, taxes levied on income and wealth in general are categorized as direct taxes, while taxes levied on expenditures are categorized as indirect taxes. A closer examination of the DST clearly demonstrates that it is neither a tax on income nor a tax on expenditures in the classical sense (Mutlu Kaya, 2020, p. 458). In this sense, the classification of the DST bears great importance. Put differently, the provisions of the DTA shall be taken as basis in case the tax in question is recognized as a tax levied on income. That is to say, an argument can be made that this tax is still collected from corporate profits (Collier & Devereux, 2017, p. 16). On the other hand, the provisions of the national legislation shall prevail in case the tax in question is recognized as a tax levied on expenditure, due to the fact that the provisions of the DTA do not cover this tax.

The rules of tax treaties pertaining to the taxation of business profits limit the power of governments to tax the activities conducted in digital environments. Therefore, it is evident that the DST, which is neither a direct tax nor an indirect tax capable of taxing digital economic activities, is a tax measure preferred by countries to ensure the taxation of digital economy income. It can be considered that this type of tax is outside the scope of application of DTAs since it is attempted to tax revenues from digital economy activities by creating a new tax type. In line with this worldwide trend Türkiye can justify the DST by citing similar examples from around the world as a precedent in the objections to be made by foreign taxpayers.

That being said, whether the DST falls under Article 2 of DTAs or whether it is a different type of tax is a matter of debate. Article 2 of MTCs defines the taxes subject to the scope of DTAs. In addition to the types of taxes levied on income and capital that are explicitly stated to be covered by the treaty at the date of signature, some taxes that enter into force after the date of signature are also stated to be covered by the treaty. Such taxes are taxes that substitute for, are levied in addition to, are of the same characteristics as, or are substantially similar to the taxes considered to be within the scope of the treaty at the time of signature. For the domestic portion of the tax base (i.e. neglecting exports and imports), one could still see a modified taxation of corporate profits.

When Türkiye is taken into consideration, the fact that the DST is levied on revenue and is assessed and collected on a monthly basis is in fact similar to the structure of indirect taxes. However, it can also be claimed that the revenues of the taxpayer companies obtained from virtual services are targeted and that it is a similar tax to the taxes levied on income in Türkiye, and therefore falls under the scope of the DTAs to which Türkiye is a party. Moreover, it can also be said that virtual environments are not defined as permanent establishments in Türkiye's DTAs, and thus Türkiye cannot levy a tax on the income generated through such environments.

As a result, there is always a risk that any step to be taken in the taxation of digital economy may conflict with the obligations arising from international tax law. It is understood that the DST is unlikely to be a long-lasting tax, as there will be no need for the DST if the global tax reform is enacted. There are substantial objections to excluding the DST from the scope of DTAs due to its controversial nature. While it is possible that the DST and similar tax rules are soon to be abolished altogether, it is not far-fetched that new tax rules based on global consensus will be implemented through a multilateral agreement.

4. Conclusion

The subject of taxes covered in DTAs is very important in today's world in which international economic relations and transactions between countries have become very complex. Since economic activities increase internationally are increasing at a dizzying pace, taxation powers between countries regarding the source and taxation of the income will be a matter of debate and possible disputes will arise. Considering that new and unusual taxes applied to digital services have increased in recent years the limits of Article 2 of the OECD MTC are inevitably being pushed. Since such types of taxes differ from the traditional understanding of income or revenue, it is difficult to classify them in terms of DTAs.

The complexity of Article 2 of the OECD MTC is often overlooked. However, when it causes unexpected interpretive problems during the implementation of DTAs, it can make DTAs inapplicable. What emerges from this confusion is that although the provisions of Article 2 are interpreted broadly, it is also possible to exclude such new taxes from the scope of DTAs. This situation frequently brings taxpayers and revenue administrations into conflict.

It is striking that although Article 2 has an important place in the implementation of DTAs, academic studies on the subject are rarely encountered. Few commentary notes are found even in the OECD MTC. Article 2 is critical in terms of the scope and interpretation and implementation of DTAs. As the diversity in tax types, especially in direct taxes, increases, it is expected that the discussions on taxes falling into the scope of DTAs will increase together with the attention and interest to Article 2.

It is clear that by abolishing the DST, which Türkiye, like many countries, applies, the coordinated implementation of the new taxation right that will arise with the MLC will be ensured. Again, it is hoped that the amount to be allocated to the source states with the MLC will be taxed by the source states and possible double taxation will be resolved with the double taxation prevention rules in the MLC.

With the MLC draft becoming available for signature in June 2024 and entering into force in 2025, OECD/G20 IF member countries shall not be able to introduce a new DST or a similar tax between January 1, 2024, and December 31, 2024, or the date the MLC enters into force. Between January 1, 2022, and the date of entry into force of the MLC, a portion of the DST collected shall be deducted from the corporate tax payable. It is expected that the abolition of the DST is likely to put an end to the disputes under Article 2 of the DTAs, at least with respect to the DST and similar taxes. Moreover, it is certain that despite all the developments at the moment the unilateral measures taken by countries will pave the way for important lawsuits and investigations in the near future.

Although Article 2(2) sets out the general rule regarding the classification of taxes, it is still difficult to adapt this rule to new types of taxes. The context is still not clear enough. Therefore, it is beneficial to adopt multilateral approaches that will reduce the risk of double taxation and ensure legal certainty. Contracting states must cooperate and mutually agree to determine the scope of Article 2 of DTAs.

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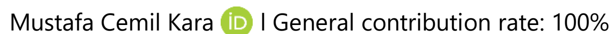
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CONFLICT OF INTEREST
The author declares no conflict of interest.

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